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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SIXTH APPELLATE DISTRICT

PAHL & MCCAY,

Plaintiff, Cross-defendant and
Respondent,

v.

WILLIAM BROOKS,

Defendant, Cross-complainant and
Appellant;

STEPHEN PAHL,

Cross-defendant and Respondent.

H043243

(Santa Clara County
Super. Ct. No. 114CV267182)

Plaintiff law firm Pahl & McCay sued William Brooks for unpaid legal fees, and Brooks cross-complained for fraud. After all evidence was presented at trial, the cross-complaint was dismissed for failing to comply with the one-year statute of limitations for attorney misconduct, and the jury returned a verdict in favor of plaintiff for the unpaid legal fees. On appeal, defendant argues his fraud claim was not subject to the one-year limitations period, and the dismissal prejudiced his defense in the original action. Finding no prejudice from the asserted error, we will affirm the judgment.

I. BACKGROUND

A. PARK PACIFIC FORECLOSURE

Defendant William Brooks is a Santa Cruz County real estate broker and developer, and is the sole owner of Brooks Properties, LLC. He conducts general real estate business through that entity, and forms additional limited liability companies to operate specific development projects.

Brooks formed a limited liability company to manage a development project in downtown Santa Cruz, and in 2007 that entity borrowed \$1.76 million from Santa Cruz County Bank (SCC Bank). He signed the loan agreement in his capacity as a member of Brooks Properties, and he and Brooks Properties personally guaranteed the loan. Originally formed as Pacific Garden Place, LLC, the entity's name was later changed to Park Pacific, LLC, and Park Pacific borrowed additional money from SCC Bank.

SCC Bank held a first lien on the downtown Santa Cruz property, and two other entities—Lighthouse Bank and Bay Side Capital Partners—acquired subordinate liens to secure outstanding loans on another of defendant's development projects, which was in financial distress. When Park Pacific could not make the monthly payments to SCC Bank, defendant and an SCC Bank representative discussed defendant having the project re-permitted and finding a buyer in lieu of foreclosure. Under that scenario, Lighthouse Bank and Bay Side Capital would each receive some money, and Brooks would recover his permitting costs through a sales commission. But the arrangement never came to fruition, and in 2012 SCC Bank foreclosed on the Park Pacific property. The bank was the foreclosing beneficiary with a \$271,657 deficiency remaining on the loan, and the junior lienholders received nothing.

B. FORECLOSURE LITIGATION

In July 2012 Lighthouse Bank, Bayside Capital Partners, LLC, and Park Pacific, LLC, collectively retained the law firm of Pahl & McCay to sue SCC Bank for fraud related to the foreclosure. Brooks Properties maintained a deposit account at

SCC Bank, and shortly after the lawsuit was filed SCC Bank seized the \$118,000 balance in that account to offset the Park Pacific loan deficiency. SCC Bank then sued Brooks for breach of guaranty to collect the remaining \$163,088 deficiency. Brooks retained Pahl & McCay to defend that action, in which defendant cross-complained against SCC Bank for conversion regarding the \$118,000. Later that year the trial court issued a writ of attachment for the \$163,088 deficiency upon the filing of an undertaking.

Brooks became increasingly disenchanted with the litigation as SCC Bank pursued his assets, and he pressed named partner Stephen Pahl (who was a founding shareholder of Lighthouse Bank, and a member of Lighthouse Bank's board of directors and loan committee chair) to settle the litigation. Dissatisfied with what he viewed as Pahl's lack of initiative, defendant extracted himself from the litigation without Pahl's assistance or knowledge, settling with SCC Bank and withdrawing from the fraud case in March 2013. The following month, Pahl & McCay sent defendant a letter terminating their representation.

C. LEGAL SERVICES LITIGATION

In June 2014 Pahl & McCay sued Brooks for breach of contract and related claims, seeking payment for legal services rendered in the lawsuit by SCC Bank. Defendant alleged as affirmative defenses that plaintiff violated the Rules of Professional Conduct and committed professional negligence by not obtaining a valid conflict waiver and by not representing him diligently and with undivided loyalty. Brooks also cross-complained against plaintiff Pahl & McCay, Stephen Pahl, and Lighthouse Bank alleging fraud and conspiracy. That cross-complaint is the subject of this appeal. Defendant alleged in the first cause of action that plaintiff and Pahl induced him to join Lighthouse Bank in suing SCC Bank and concealed that the lawsuit would likely result in a retaliatory claim against him to enforce the Park Pacific loan guaranties; that plaintiff and Pahl concealed from defendant their primary allegiance to their client Lighthouse Bank such that defendant's interests were subordinated to those of Lighthouse Bank; and that

had he “known the true facts” he would not have sued SCC Bank for fraud or engaged plaintiff to defend him in SCC Bank’s lawsuit. He sought compensation for the money seized by SCC Bank (\$118,000) and attorney’s fees related to the fraud action. The second cause of action, dismissed during trial by stipulation, alleged a conspiracy among the cross-defendants.

The case was presented to a jury in October 2015. At the close of evidence, cross-defendants successfully moved for a directed verdict on Brooks’s cross-complaint on grounds that the remaining cause of action was barred by the one-year statute of limitations in Code of Civil Procedure section 340.6, subdivision (a) for attorney wrongdoing. The jury returned a verdict for plaintiff, awarding damages of \$22,104, the outstanding balance for legal services rendered. Brooks’s motion for new trial or judgment notwithstanding the verdict was denied.

II. DISCUSSION

A. APPLICABLE STATUTE OF LIMITATIONS

The statute of limitations for fraud is three years. (Code Civ. Proc., § 338, subd. (d).) A shorter statute of limitations governs attorney malpractice claims, including constructive fraud. In “[a]n action against an attorney for a wrongful act or omission, other than for actual fraud, arising in the performance of professional services,” a one-year statute of limitations applies. (Code Civ. Proc., § 340.6, subd. (a).) “The exception for actual fraud in section 340.6 was intended to apply to intentional fraud, not constructive fraud resulting from negligent misrepresentation.” (*Quintilliani v. Mannerino* (1988) 62 Cal.App.4th 54, 69–70.)

The Civil Code defines “actual fraud” as one of two types of fraud rendering a contract voidable. (Civ. Code, §§ 1566, 1571.) Actual fraud consists of intentional misrepresentation, negligent misrepresentation, suppression of fact, a promise made without any intent to perform, and “[a]ny other act fitted to deceive,” when committed “with the intent to deceive ... or induce [another party] to enter into the contract.”

(Civ. Code, § 1572¹; *Masters v. San Bernardino County Employees Retirement Assn.* (1995) 32 Cal.App.4th 30, 41.) The acts constituting actual fraud are essentially the same as the those constituting deceit in Civil Code section 1710. (5 Witkin, Summary of Cal. Law (11th ed. 2017) Torts, § 883, p. 1208.) Fraudulent concealment, a form of intentional misrepresentation, requires a duty to disclose the concealed fact. (*Graham v. Bank of America, N.A.* (2014) 226 Cal.App.4th 594, 606.)

In contrast to actual fraud, “constructive fraud” is defined as “any breach of duty which, without an actual[] fraudulent intent, gains an advantage to the person in fault ... by misleading another to his prejudice.” (Civ. Code, § 1573.) “Constructive fraud allows conduct insufficient to constitute actual fraud to be treated as such where the parties stand in a fiduciary relationship.” (*Estate of Gump* (1991) 1 Cal.App.4th 582, 601.) “ ‘[] In its generic sense, constructive fraud comprises all acts, omissions and concealments involving a breach of legal or equitable duty, trust, or confidence, and resulting in damages to another. [Citations.] Constructive fraud exists in cases in which conduct, although not actually fraudulent, ought to be so treated—that is, in which such conduct is a constructive or quasi fraud, having all the actual consequences and all the legal effects of actual fraud.’ [Citation.] Constructive fraud usually arises from a breach of duty where a relation of trust and confidence exists.” (*Barrett v. Bank of America* (1986) 183 Cal.App.3d 1362, 1368–1369; *Tyler v. Children’s Home Society* (1994) 29 Cal.App.4th 511, 548 [a constructive fraud claim “allows relief for negligent

¹ Civil Code section 1572 provides: “Actual fraud, within the meaning of this chapter, consists of any of the following acts, committed by a party to the contract, or with his connivance, with intent to deceive another party thereto, or to induce him to enter into the contract: [¶] 1. The suggestion, as a fact, of that which is not true, by one who does not believe it to be true; [¶] 2. The positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true; [¶] 3. The suppression of that which is true, by one having knowledge or belief of the fact; [¶] 4. A promise made without any intention of performing it; or, [¶] 5. Any other act fitted to deceive.”

omissions constituting breach of duty in a confidential relationship”].) Included in the realm of constructive fraud are an attorney’s fiduciary breaches lacking fraudulent intent or motive. (*Stoll v. Superior Court* (1992) 9 Cal.App.4th 1362, 1368.)

B. THE CROSS-COMPLAINT ALLEGED ACTUAL FRAUD

Cross-defendants argue that the actual fraud exception in Civil Code section 340.6 (hereafter “section 340.6”) does not apply to Brooks’s cross-complaint because the sole claim is based on violations of professional obligations embodied in the Rules of Professional Conduct. They argue that this case comes within section 340.6’s one-year limitations period under *Lee v. Hanley* (2015) 61 Cal.4th 1225 (*Lee*) as a “ ‘claim [] whose merits necessarily depend on proof that an attorney violated a professional obligation in the course of providing professional services,’ ” regardless of how the cause of action is labeled.

Cross-defendants’ reliance on *Lee* is misplaced because that case addressed the reach of the one-year limitations period, not the scope of the express exception to that period. *Lee* did not involve a fraud claim. (*Lee, supra*, 61 Cal.4th at p. 1231.) The plaintiff in *Lee* sued her former attorney for failing to return a retainer balance, alleging breach of contract, breach of fiduciary duty, and related equitable violations (*id.* at p. 1242 [dis. opn. of Corrigan, J.]), and in the context of a demurrer the Supreme Court addressed whether “refusal to return a former client’s money after the client terminated representation was ‘a wrongful act or omission... arising in the performance of professional services’ under section 340.6(a).” (*Id.* at p. 1229.) While the Supreme Court held that the one-year time bar in section 340.6 applies to causes of action “when the merits of the claim will necessarily depend on proof that an attorney violated a professional obligation—that is, an obligation the attorney has *by virtue of* being an attorney—in the course of providing professional services” (*Lee*, at p. 1229), it expressly dissociated the actual fraud exception from that holding. “Such claims,” the court continued, “brought more than one year after the plaintiff discovers or through reasonable

diligence should have discovered the facts underlying the claim are time-barred by section 340.6(a) *unless the plaintiff alleges actual fraud.*” (*Ibid.*, italics added.) The trial court in *Lee* was found to have erred in sustaining the demurrer because the complaint could be “construed to allege” conversion which does not necessarily depend on proof that the attorney violated a professional obligation, even though the allegations, if true, may establish that the attorney also violated certain professional obligations. (*Id.* at p. 1240.) But as *Lee* did not involve a claim of actual fraud, applying its interpretation of the reach of the one-year limitations period to the actual fraud exception to that same period would effectively eliminate the exception. (*In re J.W.* (2002) 29 Cal.4th 200, 209 [principles of statutory construction dictate “that every part of a statute serves a purpose and that nothing is superfluous”].)

Cross-defendants’ reliance on *Prakashpalan v. Engstrom* (2014) 223 Cal.App.4th 1105 (*Prakashpalan*) is similarly misplaced. The court in *Prakashpalan* addressed whether the three-year limitations period in Code of Civil Procedure section 338, subdivision (d) or the three-year limitations period in Probate Code section 16460 (with different triggering acts) applied to fraud-based claims relating to an attorney’s disbursement of aggregate settlement proceeds held in a client trust account. (*Prakashpalan*, at pp. 1122–1123.) The court concluded Probate Code section 16460 (which applies to claims for breach of an express trust) governed over the more general limitations statute for fraud because the limitations period under the Probate Code was triggered by the trustee’s specific duty to provide an accounting. (*Prakashpalan*, at pp. 1124–1125.) The court went on to conclude that the statute of limitations had not been triggered because the accounting was incomplete as measured by the Rules of Professional Conduct applicable to aggregate settlements. (*Ibid.*)

Citing *Prakashpalan*, cross-defendants argue that defendant’s fraud claim falls within section 340.6’s one-year limitations period because it is premised on a breach of

professional obligations under former rule 3-310 of the Rules of Professional Conduct,² and an attorney's disclosure duties are more particularized in the rule than the Civil Code. But the fraud-based claims in *Prakashpalan* were excepted from section 340.6's one-year limitations period even though the attorney's handling of the settlement proceeds arose from the provision of professional services. (*Prakashpalan*, *supra*, 223 Cal.App.4th at p. 1122, fn. 4.) The appellate court was thus wrestling with which of two pertinent limitations statutes to apply, opting for Probate Code section 16460 as the more specific statute. The court also observed that the accounting duty imposed by the Rules of Professional Conduct relating to client trust funds was more particularized than the general duty not to omit or misrepresent facts in Civil Code section 1710. (*Prakashpalan*, at pp. 1124–1125.) But significantly, that observation was not made in the context of determining which limitations statute to apply; rather it was made in the context of determining whether the extent of the accounting provided to the plaintiffs in that case should trigger or toll the limitations period under Probate Code section 16460. (*Prakashpalan*, at p. 1125.) Here, even if the Rules of Professional Conduct prescribe Pahl & McCay's duties with greater specificity than the Civil Code, it does not follow that section 340.6's actual fraud exception should be disregarded. Actual fraud, no matter the source of duty, is exempt from section 340.6's one-year time bar.

The actual fraud exception in section 340.6 applies to all allegations of intentional fraud. (*Quintilliani v. Mannerino*, *supra*, 62 Cal.App.4th at pp. 69–70.) The relevant test is not whether the alleged attorney misconduct is necessarily related to a violation of the Rules of Professional Conduct, but whether it is alleged to arise from intentional misrepresentation or concealment of a material fact with the intent to deceive. (See Civ. Code § 1572, *ante*, fn.1.) It was an error to dismiss the cross-complaint as time-

² Former rule 3-310 of the Rules of Professional Conduct was amended and renumbered rule 1.7 in November 2018.

barred under the one-year limitations period in section 340.6(a), rather than applying that section's three-year exception for actual fraud.

C. THE ERROR WAS NOT PREJUDICIAL

Brooks argues that he alleged actual fraud, he presented evidence of actual fraud, and his proposed intentional misrepresentation and concealment jury instructions (CACI 1900 and 1901) were for actual fraud. The cross-complaint alleged fraud by concealment: That cross-defendants induced defendant to sue SCC Bank while concealing the likelihood of a retaliatory claim, and that cross-defendants' primary allegiance was to Lighthouse Bank such that defendant's interests were subordinated.

On appeal Brooks argues that he provided sufficient evidence from which a jury could have inferred the falsity of at least one of the following representations in the July 2012 engagement letter: "[W]e are unaware of the existence of any actual conflicts between you and [Lighthouse Bank]"; "we can envision potential conflicts ... [that] we do not believe ... are likely to occur"; "if an actual conflict does arise between you and [Lighthouse Bank], it may become necessary for us to withdraw from representation"; and "We will ... notify you promptly if we form the opinion that a conflict of interest exists."

Brooks points to the following evidence to demonstrate falsity: Pahl was a director, a shareholder, officer, and loan committee chair of Lighthouse Bank; Lighthouse Bank had sued Brooks in the past; Pahl regarded Brooks as someone who did not pay his bills; Pahl knew or assumed Brooks had guaranteed a loan from SCC Bank; Pahl did not warn Brooks that a lawsuit against SCC Bank could trigger action on that loan; Pahl knew Brooks's participation in a lawsuit against SCC Bank would benefit Lighthouse; and a conflict of interest actually arose when Brooks asked Pahl to settle the case, and Pahl did nothing in response.

We are mindful of the high standards governing non-suit: Conflicting evidence must be disregarded, and all legitimate inferences drawn from the evidence must be

indulged in favor of the claimant, with presumptions, inferences, and doubts being resolved in the claimant's favor. (*North Counties Engineering, Inc. v. State Farm General Ins. Co.* (2014) 224 Cal.App.4th 902, 919–920.) Even under that standard, we find the evidence of intentional concealment insufficient to support defendant's fraud claim.

The gravamen of defendant's claim was that Pahl failed to disclose his relationship with Lighthouse Bank in his engagement letter, inducing defendant to contract with Pahl & McCay for legal services. Contrary to defendant's professed ignorance of Pahl's relationship with Lighthouse Bank, the evidence at trial unequivocally established that Pahl's role had been specifically and consistently displayed to defendant in his capacity as a Lighthouse Bank shareholder. There could be no concealment given those positive disclosures.

Undisputed evidence also established both Pahl and Brooks were organizers and founding shareholders of Lighthouse Bank, which opened for business in 2007. As a shareholder Brooks received the bank's 2008-2012 annual reports, all of which identified Pahl as a member of the board of directors by name, professional capacity (senior partner and chairman of Pahl & McCay), and photograph. Brooks also received Lighthouse Bank's annual meeting notices and proxy statements with Pahl's name appearing on both documents as a current board member and secretary, and the proxy statement referencing Pahl's investments and compensation. A plaque hanging in the Lighthouse Bank lobby displays the names of the bank organizers, including both Brooks and Pahl. And Pahl had sued Brooks in 2008 on behalf of Lighthouse Bank.

"To establish prejudice, a party must show 'a reasonable probability that in the absence of the error, a result more favorable to [the party] would have been reached.' " (*Diaz v. Carcamo* (2011) 51 Cal.4th 1148, 1161.) Defendant acknowledges that evidence supporting his fraud claim, which was presented to the jury before his cross-complaint was dismissed, "also constitutes a defense to [plaintiff's] complaint for legal fees owing

on the separate and distinct theory of professional negligence and/or misconduct.” By returning a general verdict for plaintiff on the breach of contract cause of action, the jury necessarily rejected defendant’s affirmative defenses, and by rejecting those defenses, the jury also necessarily rejected his fraud claim.

Defendant argues he was prejudiced because the jury was susceptible to confusion, with the cross-complaint being dismissed after he presented his case, and “before [he] had any opportunity to clarify the issues for the jury in closing argument regarding the complaint and the cross-complaint.” But the motion for directed verdict on the cross-complaint was heard and granted on the fourth day of trial, after the close of evidence. Defendant had the remainder of that day and evening to prepare for the next morning’s closing argument and any clarification he wished to present to the jury. On this record we see no reasonable probability that a result more favorable to defendant would have been reached on either the underlying action or his cross-complaint had the latter been submitted to the jury.

III. DISPOSITION

The judgment is affirmed. Respondents shall be entitled to their costs on appeal.

Grover, J.

WE CONCUR:

Elia, Acting P. J.

Danner, J.